

FY2009 Distributions To Endowment Fund Beneficiaries

Prepared for:

Land Board Meeting

August 16, 2007

(All 2007 financial results are unaudited)



Spending Policy: Decision Time

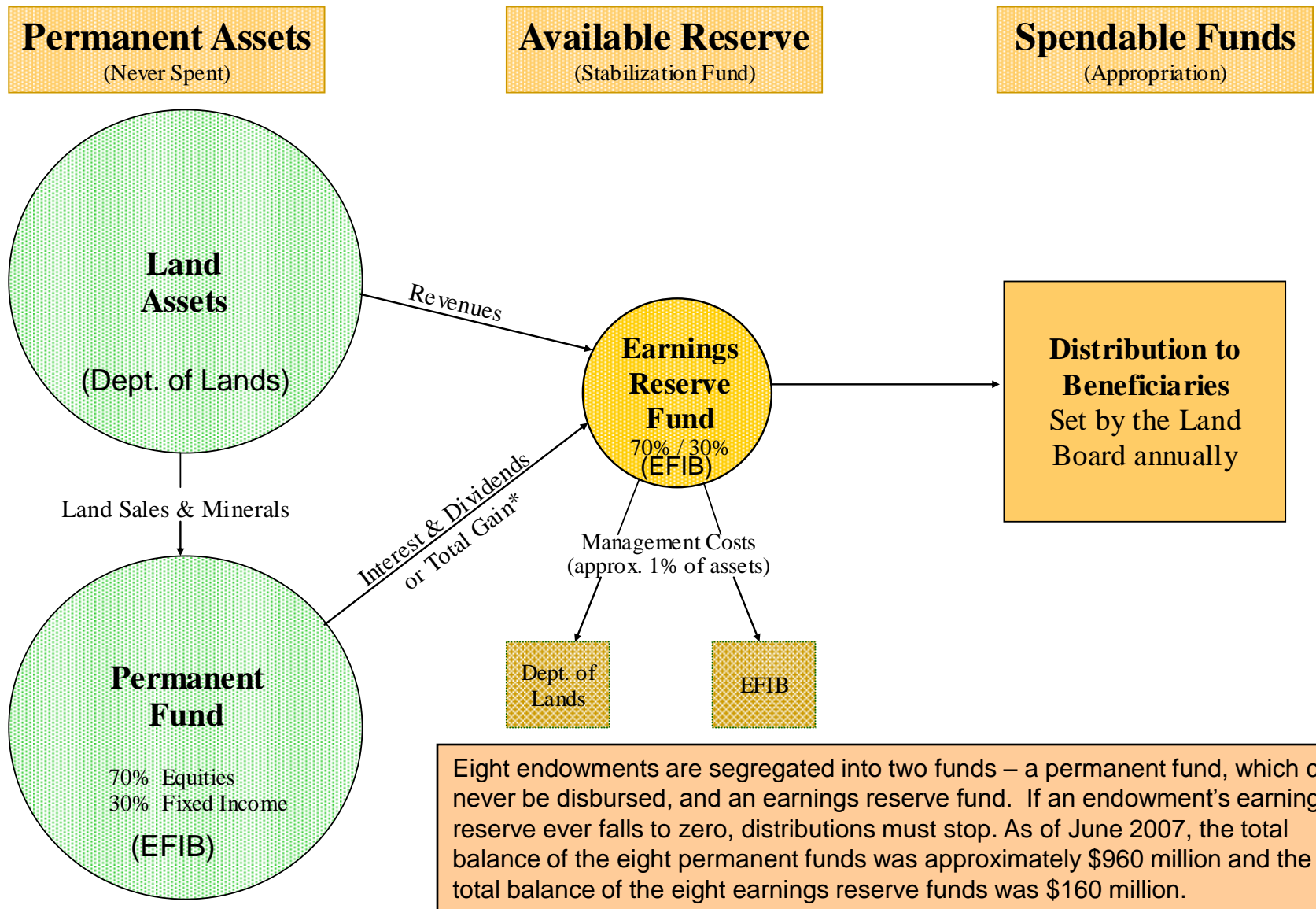
- As part of the budget process, the Land Board needs to approve endowment fund distributions for FY2009 at its August 16, 2007 meeting
 - At its 8/9 meeting, the Endowment Fund Investment Board developed a formal recommendation to the Land Board
- Approved amounts will be considered by the beneficiaries in submitting their full budgets to the Division of Financial Management September 1
- The Land Board also has option to transfer from the Earnings Reserve to the Permanent Fund of each endowment

Executive Summary

'09 Beneficiary Distributions

- Fund income has exceeded distributions to beneficiaries in recent years. As a result, Earnings Reserve balances hit new highs in FY2007, and further improvement in FY2008 is likely
- Last year, the Land Board approved a policy to distribute 5% of the 3-year average balance of the Permanent Fund (4.1% for two endowments)
- This Spending Policy, carried forward another year, results in \$42.4 million of distributions, a 9-10% increase for all endowments relative to 2008's level
- Even with this proposed increase in distributions, the likelihood of a future cutback is low
 - Distributions for all endowments remain below their forecasted Net Revenues
 - Every fund is expected to have at least three years (300%) of 2009 distributions in reserve at the end of 2008

STRUCTURE OF IDAHO'S ENDOWMENT ASSETS



* When the Permanent Fund, adjusted for inflation, exceeds its June 2000 level, only total gain over inflation will be distributed to Earnings Reserve.

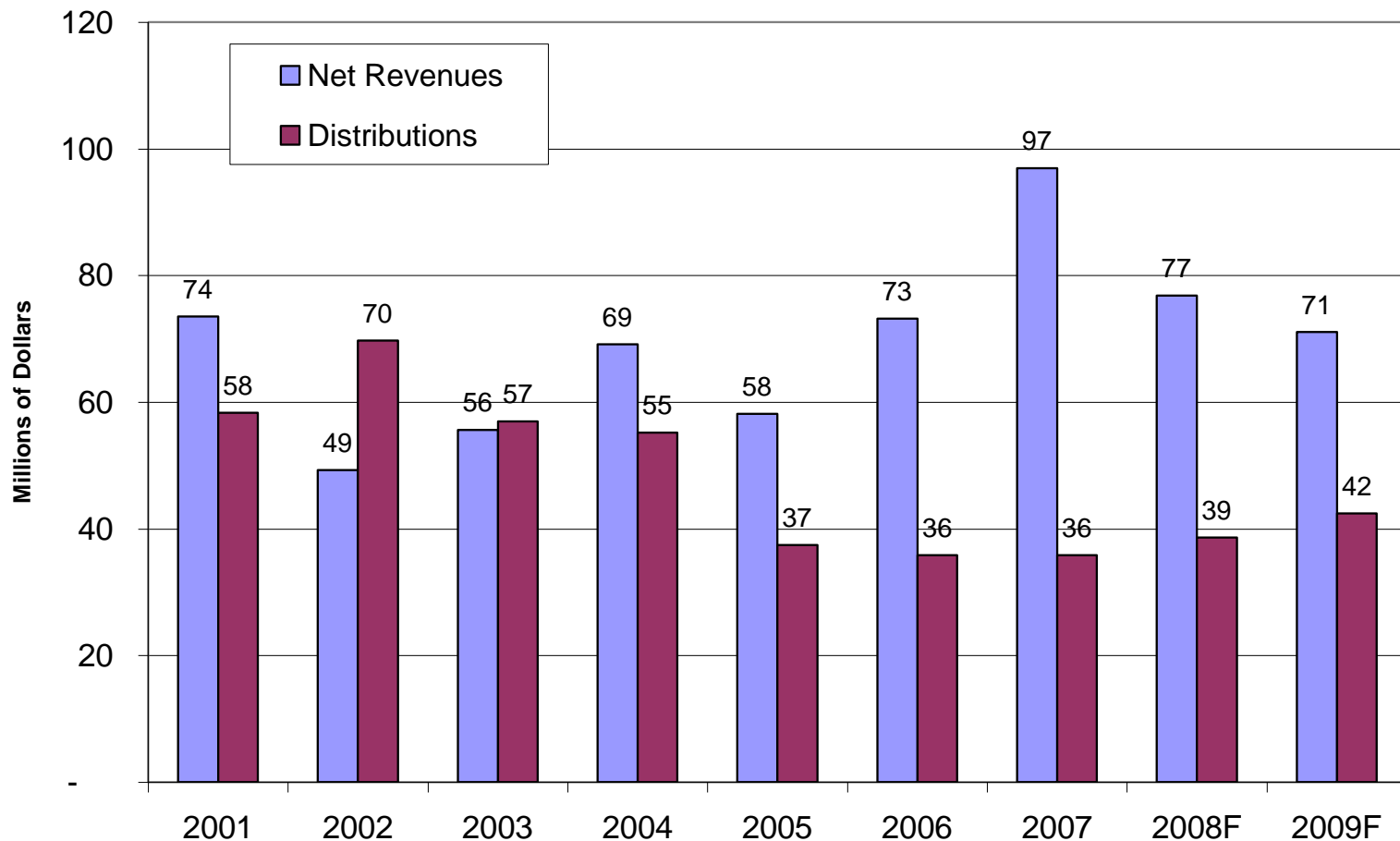
Considerations in setting distributions

- Spendable funds can only come from earnings from the land or returns from the stocks and bonds
 - Permanent funds, adjusted for inflation, can never be spent
 - Changes in earnings must eventually impact spending
- Earnings Reserve fund must absorb volatility in:
 - Interest rates (return on fixed income)
 - Stock market returns (dividends and capital gains)
 - Revenues from state lands (variation in the rate of timber harvest and the price of timber)
- A balancing act: Every dollar in current year distributions increases the likelihood of a decrease in future distributions

How much risk of a future shortfall do we want to take?

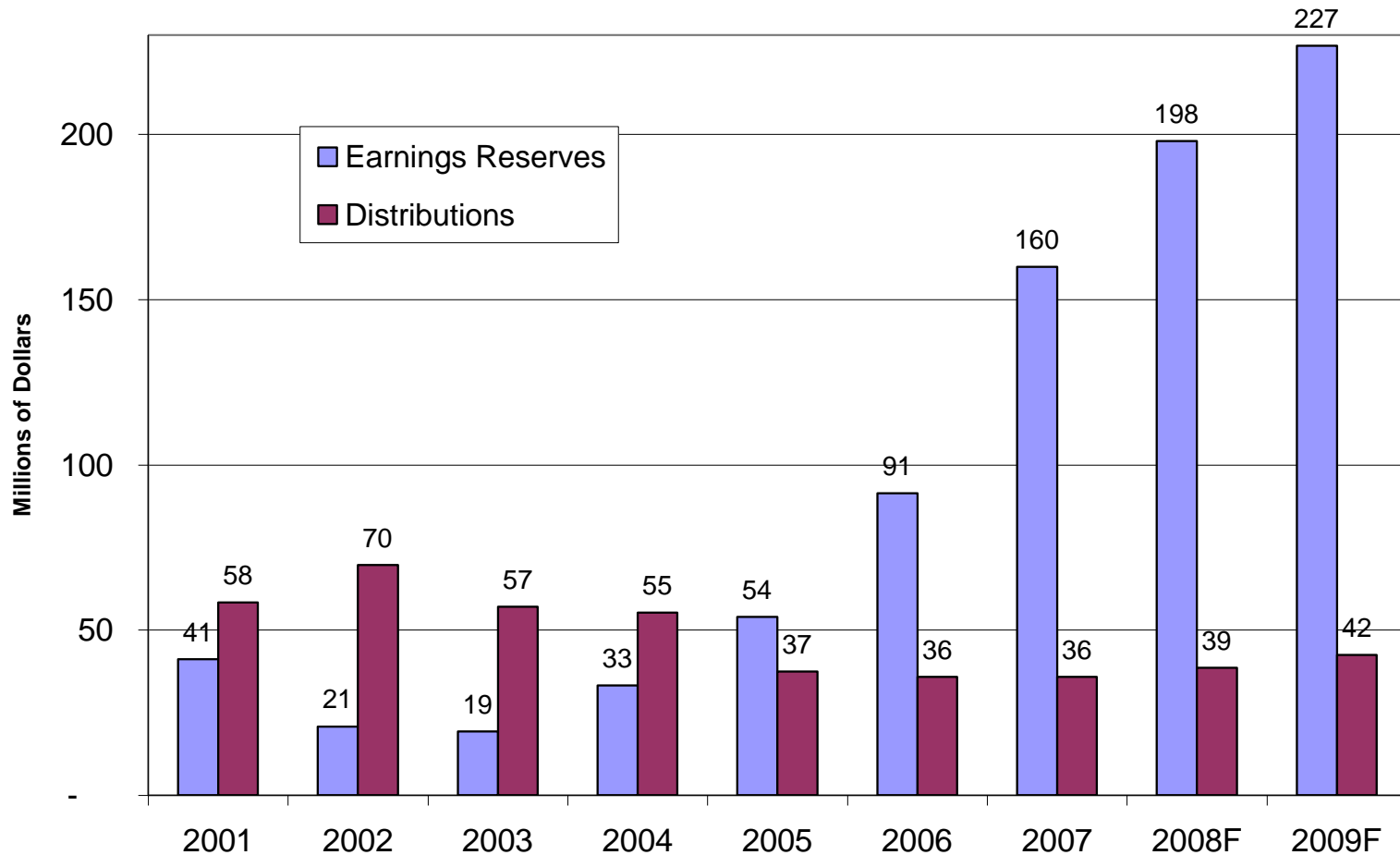
Income has exceeded distributions since 2004 – expected to continue thru at least 2009

**Net Revenues and Distributions
2001 to 2009**



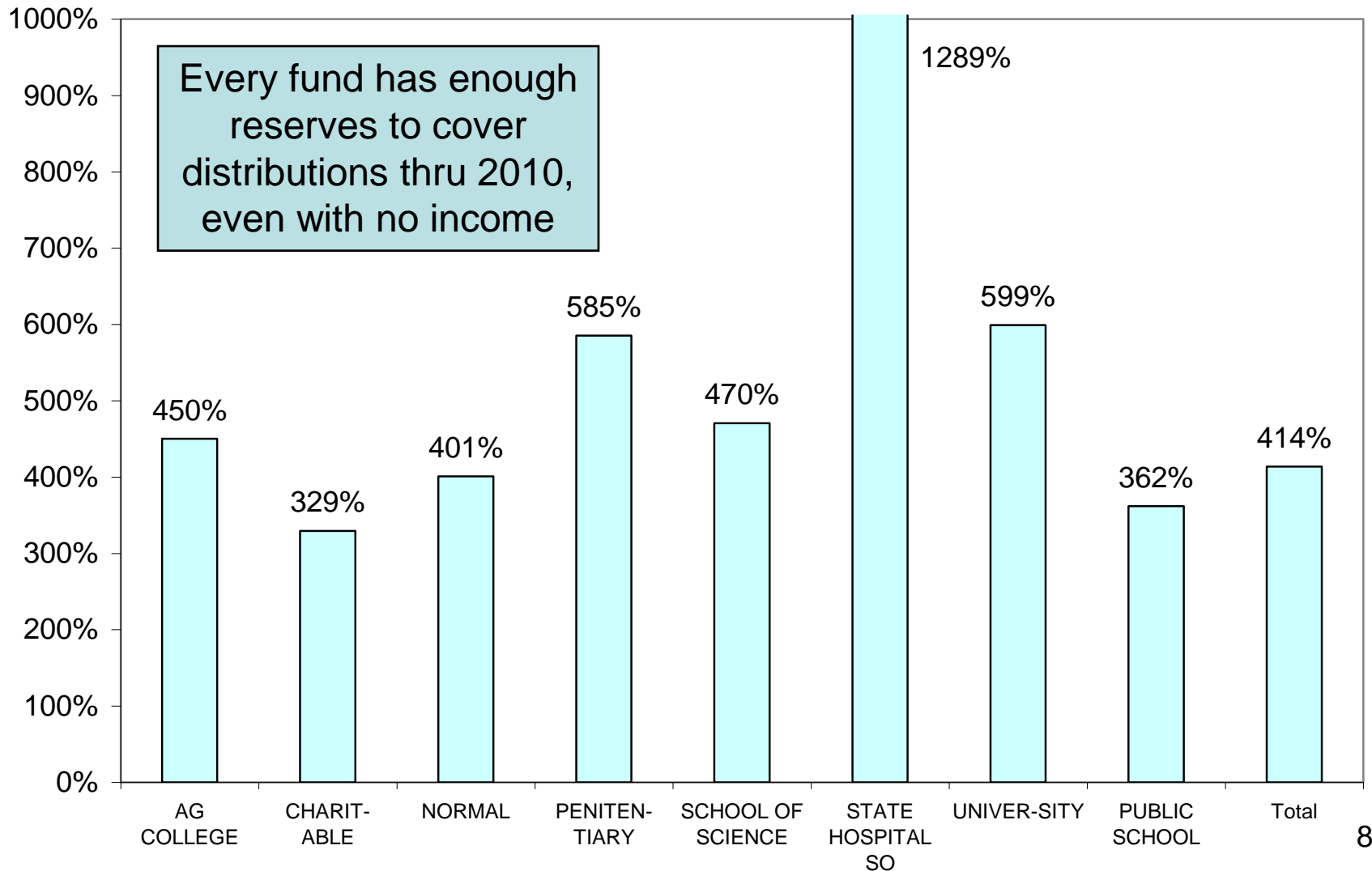
2007 reserves are at a record level and should grow thru 2009

**Reserves and Distributions
2001 to 2009**



Earnings Reserve Coverage

2007 Reserves as % of 2008 Distributions



Executive Summary

Transfers to the Permanent Fund

- The Land Board also has option to transfer funds from the Earnings Reserve to the Permanent Fund of each endowment
- These transfers should occur only when there are excess funds in Earnings Reserve, since once a transfer is made, it can never come back out
- Conclusion: At this point, no endowment has excess reserves

Current Situation vs. Long-term Expected Distributions

- As of the end of FY2007, reserves totaled \$160 million, providing significant coverage of the \$42 million recommended annual distribution
- However, our long-term strategic goal is to distribute 4% of the endowment funds plus average land revenues (over \$90 million/year)
- To comfortably distribute this strategic goal would require reserves of \$300 million, or double what is available now
 - No endowment has 100% of what is needed to cover its long-term distribution goal or target, so no transfer from Earnings Reserve to Permanent is recommended

Recommendations From the Endowment Fund Investment Board

- Recommend current Spending Policy be maintained for FY2009 distributions
 - Distributions increase in excess of inflation
 - Reserves are sufficient to support the higher level
- Recommend no transfer to the Permanent Fund
 - No endowment has “excess” reserves

Summary Proposed Distributions

Amounts in million of dollars, 2007 results are unaudited

| | Grand Total | Public Schools | Ag College** | Charit- able Institu- tions | Normal School | Peniten- tiary | School of Science | State Hospital South | University |
|--|----------------|-------------------|-----------------|--------------------------------------|------------------|-------------------|----------------------|----------------------------|------------|
| 1 Approved Land Board Spending Policy | | 5.0% | 5.0% | 5.0% | 5.0% | 4.1% | 4.1% | 5.0% | 5.0% |
| 2 Actual 2006 Earnings Reserve | 91.4 | 59.1 | 2.3 | 5.6 | 5.1 | 1.1 | 3.4 | 9.0 | 5.8 |
| 3 One-time transfer of dedicated funds | 7.4 | 5.4 | 0.1 | 0.4 | 0.3 | 0.2 | 0.4 | 0.2 | 0.3 |
| 4 2007 Distribution | (35.8) | (24.6) | (0.7) | (2.4) | (2.1) | (0.8) | (2.4) | (1.1) | (1.8) |
| 5 2007 Net revenues | 78.2 | 46.5 | 1.1 | 3.8 | 4.9 | 3.3 | 7.5 | 5.0 | 6.2 |
| 6 2007 Portfolio Gains(Losses) | 18.6 | 11.4 | 0.4 | 1.0 | 1.1 | 0.5 | 1.2 | 1.7 | 1.4 |
| 7 Change in Earnings Reserve | 68.4 | 38.7 | 0.9 | 2.9 | 4.2 | 3.2 | 6.7 | 5.8 | 6.1 |
| 8 Actual 2007 Earnings Reserve | 159.8 | 97.7 | 3.3 | 8.5 | 9.3 | 4.3 | 10.1 | 14.8 | 11.9 |
| 9 2008 Distribution (approved) | (38.6) | (27.0) | (0.7) | (2.6) | (2.3) | (0.7) | (2.1) | (1.1) | (2.0) |
| 10 2008 Net revenues (forecasted) | 76.8 | 43.9 | 2.0 | 3.5 | 4.3 | 2.5 | 8.0 | 7.5 | 5.2 |
| 11 Change in Earnings Reserve | 38.2 | 16.9 | 1.2 | 0.9 | 2.0 | 1.8 | 5.9 | 6.3 | 3.2 |
| 12 Forecasted 2008 Earnings Reserve | 198.0 | 114.7 | 4.5 | 9.4 | 11.2 | 6.0 | 15.9 | 21.1 | 15.2 |
| 13 2009 Distribution (proposed) | (42.4) | (29.7) | (0.8) | (2.8) | (2.5) | (0.8) | (2.3) | (1.3) | (2.2) |
| 14 2009 Net revenues (forecasted)* | 71.1 | 39.9 | 1.5 | 4.6 | 6.0 | 0.9 | 5.5 | 6.4 | 6.3 |
| 15 Change in Earnings Reserve | 28.7 | 10.3 | 0.7 | 1.8 | 3.5 | 0.1 | 3.2 | 5.1 | 4.1 |
| 16 Forecasted 2009 Earnings Reserve | 226.7 | 124.9 | 5.2 | 11.1 | 14.7 | 6.1 | 19.1 | 26.2 | 19.3 |
| 17 % Growth in reserves -- 2009 vs. 2007 | 42% | 28% | 59% | 31% | 58% | 44% | 90% | 77% | 62% |
| Change in distribution - 2009 Over 2008 | | | | | | | | | |
| 18 Amount (Increase)Decrease | (3.8) | (2.7) | (0.1) | (0.2) | (0.2) | (0.1) | (0.2) | (0.1) | (0.2) |
| 19 Percent Increase (Decrease) | 9.8% | 10.0% | 9.5% | 9.5% | 9.7% | 9.1% | 9.1% | 9.5% | 9.6% |
| Actual 2007 Earnings Reserve | | | | | | | | | |
| 20 Coverage of 2008 Distribution | 414% | 362% | 450% | 329% | 401% | 585% | 470% | 1289% | 599% |
| Forecasted 2008 Earnings Reserve | | | | | | | | | |
| 21 Coverage of 2009 Distribution | 467% | 386% | 567% | 332% | 442% | 762% | 683% | 1678% | 695% |

* Forecasted 2009 revenues include a \$4 million contingency reduction. Forecasts for 2008 and 2009 assume 0% portfolio return.

** Assumes Ag College moves back to 70% equity mix. 100% fixed income mix will produce 30% higher net revenues.

Coverage Info By Endowment

All dollar amounts in millions

| | <i>Distributions</i> | | | <i>Earnings Reserves</i> | | | | <i>Minimum Required Coverage****</i> |
|-------------------------|----------------------|--------------------------|--------------------|--------------------------|------------------|----------------------------------|----------------------------------|--------------------------------------|
| | <i>Actual FY2008</i> | <i>Strategic Target*</i> | <i>% of Target</i> | <i>Actual FY2007</i> | <i>Target***</i> | <i>% of FY2008 Distributions</i> | <i>% of Target Distributions</i> | |
| Public Schools | 27.0 | 59.2 | 46% | 97.7 | 171.6 | 362% | 165% | 290% |
| Ag College | 0.7 | 2.3 | 32% | 3.3 | 7.9 | 450% | 145% | 350% |
| Charitable Institutions | 2.6 | 5.9 | 43% | 8.5 | 16.4 | 329% | 143% | 275% |
| Normal School | 2.3 | 6.7 | 34% | 9.3 | 20.5 | 401% | 138% | 305% |
| Penitentiary | 0.7 | 2.6 | 29% | 4.3 | 10.5 | 585% | 167% | 410% |
| School of Science | 2.1 | 7.7 | 28% | 10.1 | 29.3 | 470% | 131% | 380% |
| State Hospital South | 1.1 | 6.8 | 17% | 14.8 | 19.8 | 1289% | 217% | 290% |
| University | 2.0 | 7.1 | 28% | 11.9 | 24.8 | 599% | 169% | 350% |
| Total | 38.6 | 98.2 | 39% | 159.8 | 300.6 | 414% | 163% | 300% |

* Target distributions and reserves represent the Strategic Plan to distribute, long-term, 4% of the endowment funds plus expected land revenues

** Reserves required to distribute at levels targeted in the Strategic Plan, based on the required minimum coverage

*** Based on expected volatility of land revenues plus a 200% safety margin

Coverage of long-term levels of distributions does not exceed the minimum required